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CHARLES ELMORE CROPLEY
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Supreme Court of the United States

OCTOBER TERM, 1942.

No. 508

VIM SECURITIES CORPORATION,
Petitioner,

—v.—

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND SUPPORTING BRIEF.

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IN THE

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VIM SECURITIES CORPORATION,
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COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND SUPPORTING BRIEF.

TO THE HONORABLE SUPREME COURT OF THE UNITED STATES:

Vim Securities Corporation prays that a writ of certiorari issue to review the judgment and decree of the United States Circuit Court of Appeals for the Second Circuit (R. 72) entered in the above cause on August 6, 1942, affirming a decision of the United States Board of Tax Appeals (R. 23-43).

OPINIONS BELOW.

The opinion of the United States Board of Tax Appeals (R. 23-43) is reported in 43 B. T. A. 759. The opinion of the Circuit Court of Appeals (R. 67-72) is not yet reported but may be found at Paragraph 9602, Vol. 4, 1942 Edition, Commerce Clearing House Tax Service.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on August 6, 1942 (R. 72). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. A. § 347).

QUESTIONS PRESENTED.

The case presents the following questions:

(1) Whether gain realized by the taxpayer as a result of receiving an award for the condemnation of its property was subject to the provisions of Section 112(f) of the Revenue Act of 1936, excepting gain from recognition where an award is expended in the acquisition of other property similar or related in service or use to the property condemned, or in the acquisition of control of a corporation owning such other property.

(2) Whether the taxpayer was engaged in business during the year 1936 within the meaning of the tax on excess profits.

The Court below held that the petitioner was not entitled to the benefits of the relief provisions of Section 112(f) of the Revenue Act of 1936 and that the corporation was engaged in business during the year 1936.

STATUTES INVOLVED.

Revenue Act of 1936: 49 Stat. 1681 (26 U. S. C. 112).

Sec. 112. Recognition of Gain or Loss.

> "(f) Involuntary conversions. If property (as a result of its destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) is compulsorily or involuntarily converted into property similar or related in service or use to the property so converted, or into money which is forthwith in good faith, under regulations prescribed by the Commis-

sioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, no gain or loss shall be recognized. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended."

Section 105(a) of the Revenue Act of 1935, as amended by Section 401 of the Revenue Act of 1936 provides as follows:

> "Section 105(a). For each year ending June 30, beginning with the year ending June 30, 1936, there is hereby imposed upon every domestic corporation with respect to carrying on or doing business for any part of such year an excise tax of $1 for each $1,000 of the adjusted declared value of its capital stock."

Section 106 of the Revenue Act of 1935 as amended by Section 402 of the Revenue Act of 1936 imposes an excess profits tax on every corporation which is subject to capital stock tax under Section 105 of the Revenue Act of 1935 as amended by Section 401 of the Revenue Act of 1936.

STATEMENT OF FACTS.

The Court of Appeals found the following facts (R. 68-69):

> Prior to June 28, 1935, Vim Securities owned a warehouse at 16 Concord Street, Brooklyn. The City of New York brought a condemnation proceedings to acquire title to the property. Title passed to the City on June 28, 1935, and under final decree of the New York Supreme Court, dated July 14, 1936, the award was fixed at $85,000 and interest and became payable on that date. The stock of Vim Securities was owned by four brothers named Kassover in equal proportions.
>
> Prior to June 28, 1935, Vim Electric, a corporation whose stock, like that of Vim Securities, was shared equally by the four Kassover brothers, occupied 16 Concord Street as tenant of Vim Securities, and after the condemnation continued to occupy them until the

latter part of December, 1935, under a temporary arrangement with the city. There- [fol. 69] after it moved to 325-27 Gold Street, Brooklyn, which it has since occupied, paying rent therefor to Gold Street Corporation, the formation of which we shall speak of later.

After the condemnation, and on August 19, 1935, one of the Kassovers made a contract with the Dime Savings Bank of Brooklyn to purchase 325-27 Gold Street for $110,000, of which $10,000 was to be paid on the execution of the contract, and $100,000 on the delivery of the deed in October. His purpose was to obtain a new warehouse in place of the one condemned. On October 4, 1935, Kassover assigned this contract to Gold Street Corporation, which had been organized by the Kassover brothers on October 1, 1935, in order to take title to the Gold Street premises. The stock of the corporation, like that of the other two companies, seems to have been owned by the Kassover brothers in equal shares. Its income tax return listed them as each owning 12½ shares and as its sole stockholders.

The initial payment of $10,000 required under the contract to purchase 325-27 Gold Street was made by checks of Vim Securities for $2,000 and of Vim Electric for $8,000. The payment of the balance of $100,000 necessary to complete the purchase was made on October 5, 1935, by the personal check of one of the Kassovers for $100,000, which was derived from deposits in his bank account of three checks of Vim Electric (drawn for the purpose) of which, as we have said, the four Kassovers were the sole stockholders. On November 27, 1935, Vim Securities, which had originally advanced $2,000 toward the purchase, delivered its check for $8,000 to Vim Electric in order to refund the latter's past contribution of $8,000. On January 29, 1936, Vim Securities made a further payment to Vim Electric of $5,000. On October 9, 1936, the City of New York paid the award of $85,000 and interest. This was done by paying [fol. 70] off a mortgage of $12,000 on 16 Concord Street and by paying the balance of $79,604.08 to Vim Securities whose property had been condemned. Vim Securities thereafter made further reimbursement to Vim Electric for the advances, made by the latter to purchase the Gold Street

property, by drawing its checks to Vim Electric between January and June, 1937, inclusive, for various sums aggregating $85,000, and by making a final payment of $10,000 on July 12, 1937.

The books of Vim Securities charged Vim Electric both with the $2,000 payment that Vim Securities had made to the Dime Savings Bank toward the $10,000 deposit for the purchase of 325-27 Gold Street and with the $8,000 originally paid by Vim Electric and later refunded to it by Securities.

The books of Vim Electric carried its payments to purchase Gold Street as an account receivable from Gold Street Corporation, and the latter carried them as an account payable to Vim Electric. It may be inferred that when Vim Securities reimbursed Vim Electric for the payments to purchase Gold Street, it thereby acquired the account receivable due Vim Electric from the Gold Street Corporation and became the creditor of the latter in the amount of $110,000. Gold Street Corporation carried debit and credit items of $5,500 on its books, designated as "interest Vim Electric Co., Inc.," and apparently representing interest accrued on Vim Electric's advances up to the time Vim Electric Company was reimbursed by Vim Securities. The books of Gold Street Corporation also carried the items "Real Estate, Taxes, Insurance, Interest on Mtges., Taxes, Depreciation," all representing expenses of the Gold Street Corporation.

SPECIFICATION OF ERRORS TO BE URGED.

The Court below erred:

(1) In holding that the petitioner was not entitled to the benefit of the relief provisions of Section 112(f) of the Revenue Act of 1936 and that the gain resulting from the award under the condemnation proceedings was taxable in full to the petitioner corporation.

(2) By holding that the relief provisions of Section 112(f) of the Revenue Act of 1936 were inapplicable to the petitioner because the property purchased to replace the property condemned was bought in the name of Gold Street Corporation, whose stock was owned by the stockholders of the petitioner corporation in equal proportions.

(3) In holding that the decision of this Court in *Higgins* v. *Smith*, 308 U. S. 473 (involving gain on the sale of stock to a wholly owned corporation) should also be applied in cases such as the one at bar involving statutory relief provisions.

(4) In interpreting the relief provisions of Section 112(f) of the Revenue Act of 1936 strictly rather than liberally and resolving all doubts against the taxpayer.

(5) In holding that during the year 1936 the petitioner corporation was engaged in business and subject to excess profits tax even though during the year 1935 it had been deprived of its real property by condemnation proceedings and in 1936 merely received the condemnation award which was later paid to a creditor who advanced the money for the purchase of the property used in replacement.

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT.

1. The decision of the Circuit Court of Appeals herein on both of the issues involved does not accord in principle with decisions of this Court and is in conflict with decisions of other Circuit Courts of Appeal.

2. The Circuit Court of Appeals had decided an important question of Federal tax law which has not been but should be settled by this Court.

CONCLUSION.

It is therefore respectfully submitted that this petition should be granted.

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BRIEF IN SUPPORT OF PETITION.

I.

THE DECISION OF THE COURT BELOW ON THE QUESTION WHETHER PETITIONER WAS ENTITLED FOR THE YEAR 1936 TO THE BENEFITS OF THE RELIEF PROVISIONS OF SECTION 112(f) OF THE REVENUE ACT OF 1936 IS NOT IN ACCORD IN PRINCIPLE WITH THE DECISIONS OF THIS COURT AND IS IN CONFLICT WITH DECISIONS OF OTHER CIRCUIT COURTS OF APPEAL.

(a) It is well settled that Section 112(f) of the Revenue Act of 1936 is a relief provision. *Washington Railway & Electric Co.* v. *Commissioner* and cases cited therein, 40 B. T. A. 1229.

A relief provision should be construed liberally to effect its purpose. *Helvering* v. *Bliss*, 293 U. S. 144; *U. S.* v. *Pleasants*, 305 U. S. 357, 363; *Gould* v. *Gould*, 245 U. S. 151.

The Court of Appeals construed this section of the statute strictly rather than liberally and accordingly its decision does not accord with the law as established by this Court in connection with statutory relief measures. The Court below found both as a matter of fact and law that the Gold Street property was acquired for a use similar to that of the Concord Street warehouse which had been owned by the petitioner prior to condemnation. However, the Circuit Court of Appeals decided that the petitioner was not entitled to relief because title to the Gold Street property acquired in place of the Concord Street property was taken in the name of Gold Street Corporation. The Court below relied on the case of *Higgins* v. *Smith*, 308 U. S. 473. We think that *Higgins* v. *Smith*, *supra*, and similar cases involving the creation of corporate entities to avoid taxes have no application to a remedial statute such as Section 112(f) and can have no possible bearing here. There the taxpayer sold securities to his wholly owned self-created corporation at a loss to secure tax deductions. The loss was disallowed by the Court. Here there was no attempt to avoid tax by the formation of the

Gold Street Corporation and the taxpayer in good faith paid over the award money in connection with the replacement of the property.

(b) The Court below followed the form rather than the substance of the transaction involved and held that the petitioner neither acquired the Gold Street property nor the control of the Gold Street Corporation.

The Court below found as a fact that the stock of the Gold Street Corporation, the stock of the petitioner and the stock of Vim Electric Company, the tenant, was owned by the same parties, the Kassover Brothers, in equal shares (R. 68). In its opinion (R. 71) the Court referred to *United States* v. *The Brager Building & Land Corporation*, 124 F. (2d) 349, 351. In that case the United States Circuit Court of Appeals for the Fourth Circuit held that where a corporation was organized for the sole purpose of taking title to real estate for the convenience of a partnership which controlled the corporation, that the income from the property was attributable to the partnership and that the corporation was a mere conduit. In that case the Court followed the substance of the transaction rather than the form.

> "Taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed * * *."
>
> *Griffiths* v. *Commissioner*, 308 U. S. 355, 357-8;
> *U. S.* v. *The Brager Building & Land Corporation*, *supra*.

In *North Jersey Title Ins. Co. et al.* v. *Commissioner of Internal Revenue*, 84 F. (2d) 898 (C. C. A. 3), the Circuit Court of Appeals held:

> "Where title insurance company invested in mortgages on vacant lots which were represented as being improved and created subsidiary corporate structure for purpose of dealing with such mortgaged property in order to avoid disastrous results to title insurance business which might follow if public learned of the transactions and not in order to escape taxation, sub-

sidiary corporate structure was not separate entity for purpose of taxation, and its losses or gains could be considered as losses or gains of title insurance company."

In the course of its opinion the Court stated in part as follows:

* * * * *

"The principle that substance and not form should control in the application of income tax law is fundamental. Fictional corporate camouflage cannot be made the device to escape taxation. On the other hand, equal equity demands that the creation of a subsidiary corporate structure with no purpose of evading tax but solely for the purpose of meeting the exigencies of a serious and possible fatal financial situation should not be regarded as the birth of a new entity completely unidentified with the former for taxing purposes, particularly under the peculiar circumstances surrouning the instant case."

* * * * *

We think that the decision of the Court below is in conflict with the decision of the Third Circuit in *North Jersey Title Ins. Co. et al.* v. *Commissioner of Internal Revenue, supra.* Furthermore the decision of the Court below appears to be in conflict with its own decision in *Munson S.S. Line* v. *Commissioner,* 77 F. (2d) 849 (C. C. A. 2). That case involved a statutory relief provision and the Court held that substance and not form should control and that corporate entities should be disregarded.

The decision of the Circuit Court is also in direct conflict with the decision of the Fourth Circuit in *United States* v. *The Brager Building & Land Corporation, supra,* and the cases cited therein.

This Court has held on several occasions that in tax cases the separate identity of corporations may be disregarded. *Southern Pacific Co.* v. *Lowe,* 247 U. S. 330, 38 S. Ct. 540, 62 L. Ed. 1142; *Gulf Oil Corp.* v. *Lewellyn,* 248 U. S. 71, 39 S. Ct. 35, 63 L. Ed. 133; *New Colonial Ice Co.* v. *Helvering,*

292 U. S. 435, 54 S. Ct. 788, 78 L. Ed. 1348; *Griffiths* v. *Commissioner, supra.*

The case of *Abrams Sons Realty Co.* v. *Commissioner of Internal Revenue,* 40 B. T. A. 653, illustrates the point and presents a situation where the respondent proceeded on a theory exactly opposite to his action in the case at bar. There property was conveyed to a corporation for the benefit of the creditors of the transferors and to permit the corporation to receive the proceeds of a pending condemnation proceeding and to distribute these proceeds to the creditors. The Commissioner of Internal Revenue taxed the corporation as the owner of the property and the recipient of the gain from the condemnation proceeding. The Board overruled the Commissioner and held that the corporation was a mere conduit for the proceeds of the condemnation award and that the original owners of the property (transferred to the corporation) were taxable on the proceeds of the condemnation. The Board relied on the *112 West 59th Street Corporation* v. *Helvering,* 68 F. (2d) 397, and *Central Life Society* v. *Commissioner,* 51 F. (2d) 941.

The Board reached a similar conclusion and disregarded the corporate entities involved in *Moline Properties, Inc.* v. *Commissioner,* 45 B. T. A. No. 105 (November 7, 1941); *J. L. McInerney* v. *Commissioner,* 29 B. T. A. 1, affirmed 82 F. (2d) 665; *Mark A. Mayer,* 36 B. T. A. 117; and *Stewart Forshay,* 20 B. T. A. 537.

The term "controlled" is defined by Article 45-1 of Respondent's Regulations 94, promulgated under the Revenue Act of 1936 as follows:

> "(3) The term 'controlled' includes any kind of control, direct or indirect, whether legally enforceable, and however exercisable or exercised. It is the reality of the control which is decisive, not its form nor the mode of its exercise. A presumption of control arises if income or deductions have been arbitrarily shifted.
>
> "(4) The term 'controlled taxpayer' means any one of two or more organizations, trades, or businesses

owned or controlled directly or indirectly by the same interests.

"(5) 'Group' or 'group of controlled taxpayers' means the organizations, trades, or businesses owned or controlled by the same interests. * * *"

Therefore, under the respondent's own published definition of the term "controlled", the Gold Street Corporation was controlled by the petitioner inasmuch as the stock of both corporations was owned in equal proportions by the same stockholders and the officers and directors of both corporations were identical.

Corporations are even deemed to be affiliated for the purpose of consolidated returns if substantially all of the stock of two or more domestic corporations is owned or controlled by the same interests. *Handy & Harman* v. *Burnet*, 52 S. Ct. 21, 284 U. S. 136. Here, as the Circuit Court found (R. 70), there was a complete stock ownership in all of the corporations involved by four individuals in equal proportions. We believe that the decision of the Court below is out of line with and in conflict with the decisions hereinabove set forth. The doctrine of *Higgins* v. *Smith, supra*, should not be extended to a situation involving a relief provision and relief denied because title to replacement property is taken in the name of a corporation owned and controlled by the same interests as the corporation which received the award.

(c) The attention of the Court is respectfully directed to the fact that the Court below was in doubt on the question whether corporate entity should be disregarded here for the Court said (R. 71):

"* * * But even if it be assumed that the various intercorporate transactions we have mentioned were illusory (see *United States* v. *Brager Building & Land Corporation*, 125 F. (2d) 349, 351), and that Gold Street Corporation was a sham or a mere passive trustee for Vim Securities, still the latter cannot be said to have complied with Section 111(f) of the Revenue Act of 1936, for it did not 'forthwith' expend its award

> in the acquisition either of the Gold Street property or of the control of Gold Street Corporation. * * * "

We think that it is clear from the record that the petitioner did "forthwith" expend the award money in connection with the acquisition of the Gold Street property to replace the Concord Street property condemned. The Court below found as a fact that title passed to the City of New York on June 28, 1935 by reason of the condemnation and that on August 19, 1935 a contract was executed for the purchase of the Gold Street property to replace the property condemned (R. 68). The initial payment of $2,000 was made by the petitioner corporation and the balance of the $10,000 down payment for the property, $8,000, was advanced by the Vim Electric Company in the Fall of 1935. On November 27, 1935 the petitioner delivered its check for $8,000 to Vim Electric in order to refund the latter's advance of $8,000 (R. 68-69). Also a further payment to Vim Electric was made by the petitioner on January 29, 1936. It is true that the balance of the purchase price was advanced by the Vim Electric Company (R. 68-69), but the award was not received by petitioner until the Fall of 1936, over a year after the original condemnation. Although the award was not received for more than a year the property condemned was immediately replaced and after the award was received the creditor, Vim Electric Company, was paid off in monthly installments beginning in January of 1937.

Here again we believe that the relief provisions should be liberally rather than strictly construed and that the condemned property was "forthwith" replaced and payments to the advancing creditor were "forthwith" made after the receipt of the award within the meaning of the statute.

We cannot find that the meaning of the term "forthwith" has been defined by the Courts with relation to Section 112(f) of the Revenue Act of 1936. However, the term has been defined by the Board of Tax Appeals in the leading case decided by the Board on this particular relief provision of the statute, *Washington Railway & Electric Co.* v. *Commis-*

sioner, 40 B. T. A. 1229. In that case at page 1258 of 40 B. T. A. the Board stated:

> "* * * Even though we consider the situation here covered by that part of the statute having to do with the conversion of the property into money which is forthwith expended in the acquisition of similar property, we can see no reason compelling us to make so illiberal a construction of the statute as to conclude that the relief provided by it and intended by Congress is not available to petitioner. To do so it would be necessary to construe the word 'forthwith' as meaning 'afterwards,' that is, after the actual conversion and the receipt of the award. The dictionary defines 'forthwith' as follows: Immediately; without delay; directly; hence, within a reasonable time under the circumstances of the case; promptly and with reasonable dispatch. According to this definition it seems apparent that Congress, by the use of the word 'forthwith,' meant to provide that the expenditure of money resulting from the involuntary conversion of property in the acquisition of similar property must be made with some immediate chronological relationship to the conversion thereby guarding against such a long delay *after* the conversion as to raise a doubt whether the purchase of similar property was actually and in good faith a replacement, or was an additional investment. If there is that immediate chronological relationship between the expenditure for replacement and the condemnation or threat thereof, it is immaterial that the expenditure for replacement immediately preceded the payment of the compensation or immediately followed it. Upon this general subject see *August Buckhardt*, 32 B. T. A. 1272; *M. J. Caldbeck Corporation*, 36 B. T. A. 452. * * *"

The Court below found (R. 70) that the replacing property was acquired for use similar to that of the property condemned and we respectfully submit that the action of the petitioner was in accord with the meaning of the word "forthwith" as that term has been defined by the Board of Tax Appeals in a liberal construction of the statute.

The substance of the petitioner's position is that a relief provision of this character should be liberally construed and that the Court below erred by its strict construction and the resolving of all doubts against the taxpayer.

II.

THE DECISION OF THE COURT BELOW THAT THE PETITIONER WAS "CARRYING ON OR DOING BUSINESS" DURING THE YEAR 1936 IS NOT IN ACCORD WITH DECISIONS OF THIS COURT AND IS IN CONFLICT WITH DECISIONS OF THE OTHER CIRCUIT COURTS OF APPEAL.

Section 105(a) of the Revenue Act of 1935, as amended by Section 401 of the Revenue Act of 1936 provides for a capital stock tax on all domestic corporations with respect to carrying on or doing business.

Section 106 of the Revenue Act of 1935 as amended by Section 402 of the Revenue Act of 1936 imposes an excess profits tax on every corporation which is subject to capital stock tax.

Accordingly, the test for the imposition of an excess profits tax is whether a corporation is "carrying on or doing business."

It appears well settled that a corporation which merely receives the income earned by its assets which it owns and distributes that income among stockholders is not "engaged in or doing business." *Zonne* v. *Minneapolis Syndicate,* 220 U. S. 187, 31 S. Ct. 361, 55 L. Ed. 428; *McCoach* v. *Minehill, etc. R. Co.,* 228 U. S 295, 32 S. Ct. 842, 56 L. Ed. 1269; *U. S.* v. *Emery, etc. Co.,* 237 U. S. 28, 35 S. Ct. 499, 59 L. Ed. 825; *Rose* v. *Nunnally Investment Company,* 22 F. (2d) 102 (C. C. A. 5). The mere ownership and leasing, without operation of a parcel of real estate is not such a transaction of business as to subject the owner to excess profits tax. *Sears* v. *Hassett,* 111 F. (2d) 965 (C. C. A. 1); *Kingkade Hotel Co.* v. *Jones,* 30 F. Supp. 508.

In *Zonne* v. *Minneapolis Syndicate, supra,* this Court stated in part as follows:

> "The corporation involved in the present case, as originally organized, and owning and renting an office building, was doing business within the meaning of the statute as we have construed it. Upon the record now presented we are of opinion that the Minneapolis Syndicate, after the demise of the property and reorganization of the corporation, was not engaged in doing business within the meaning of the act. It had wholly parted with control and management of the property; its sole authority was to hold the title subject to the lease for 130 years, to receive and distribute the rentals which might accrue under the terms of the lease, or the proceeds of any sale of the land, if it should be sold. The corporation had practically gone out of business in connection with the property, and had disqualified itself by the terms of reorganization from any activity in respect to it."

The record herein clearly shows that the taxpayer's building was condemned in 1935 and that in 1936, the year here involved, the taxpayer received the award and merely passed the award money on to its tenant for money advanced to replace the building originally owned. The Court below held that the taxpayer should be deprived of the benefits of Section 112(f) because the building purchased in replacement was purchased in the name of another corporation. Thus, under the Court's decision on the relief point, the petitioner herein did not even own a building in 1936. It became merely an empty shell, neither owning nor operating property.

The attorney fees of $2,050.39, expended by the petitioner in 1936, were paid to the attorney who represented the petitioner in the condemnation proceedings (Petitioner's Exhibit 2). So it becomes clear that the attorney fees were not in connection with the operation of the corporation as a going business but rather were fees which were incurred in the very proceeding which depleted the petitioner of its real property.

It is therefore respectfully submitted that the decision of the Court below is not in accord with the decisions of this Court in *Zonne* v. *Minneapolis Syndicate, supra; McCoach* v. *Minchill, supra* and *U. S.* v. *Emery, supra.* Also the decision is in conflict with the decisions of the Fifth Circuit in *Rose* v. *Nunnally Investment Company, supra,* and the First Circuit in *Sears* v. *Hassett, supra.*

III.

THE CIRCUIT COURT OF APPEALS HAS DECIDED AN IMPORTANT QUESTION OF FEDERAL TAX LAW WHICH HAS NOT BEEN BUT SHOULD BE SETTLED BY THIS COURT.

The relief provisions of Section 112(f) of the 1936 Act and the similar provisions of other Revenue Acts have, as pointed out hereinabove, been considered on numerous occasions by the Board of Tax Appeals. However, there have been few Court decisions upon the subject and the questions involved therein have never been passed upon by this Honorable Court. We have demonstrated hereinabove that the relief provisions of Section 112(f) of the 1936 Act, involving condemnation awards should be construed liberally rather than strictly as was done by the Court below.

The attention of this Court is respectfully directed to the fact that in denying the relief provisions of the pertinent section of the statute to the petitioner, the Circuit Court of Appeals relied on the doctrine of *Higgins* v. *Smith, supra.* We think that it is important that this Court settle the question whether the doctrine of *Higgins* v. *Smith, supra,* should be extended and applied to such circumstances as are here involved and where relief provisions are to be interpreted. Compare *Griffiths* v. *Commissioner, supra,* and *United States* v. *The Brager Building & Land Corporation, supra.*

It also appears that on the issue involving the question whether the petitioner was "doing business" the decision of

the Court below stands practically alone on this important matter. We think it clear that if the corporation is to be denied relief under Section 112(f) on the theory that the Gold Street property was not purchased in its name, then certainly it cannot be said that the petitioner was doing business within the taxable year after having been deprived of its holdings by reason of the condemnation proceedings.

It is therefore respectfully submitted that the petition should be granted.

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495958—42

In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 508

VIM SECURITIES CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 23–42) is reported in 43 B. T. A. 759. The opinion of the circuit court of appeals (R. 67–71) is reported in 130 F. (2d) 106.

JURISDICTION

The judgment of the circuit court of appeals was entered on August 6, 1942 (R. 72). The petition for a writ of certiorari was filed on November

2, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

(1) Whether gain realized by petitioner upon receipt of an award for the condemnation of its property is subject to the nonrecognition provisions of Section 112 (f) of the Revenue Act of 1936.

(2) Whether petitioner carried the burden of proving that it was not engaged in business within the meaning of the tax on excess profits.

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1935, c. 829, 49 Stat. 1014:

> SEC. 105. CAPITAL STOCK TAX.
>
> (a) For each year ending June 30, beginning with the year ending June 30, 1936, there is hereby imposed upon every domestic corporation with respect to carrying on or doing business for any part of such year an excise tax * * *.
>
> * * * * *
>
> SEC. 106. EXCESS-PROFITS TAX.
>
> (a) There is hereby imposed upon the net income of every corporation for each income-tax taxable year ending after the close of the first year in respect of which it is taxable under section 105, an excess-profits tax equal to the sum of the following:
>
> * * * * *

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section

* * * * *

(f) *Involuntary Conversions.*—If property (as a result of its destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) is compulsorily or involuntarily converted into property similar or related in service or use to the property so converted, or into money which is forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, no gain or loss shall be recognized. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended.

* * * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 112 (f)–1. *Reinvestment of proceeds of involuntary conversion.*—In order to

avail himself of the benefits of section 112 (f) it is not sufficient for the taxpayer to show that subsequent to the receipt of money from a condemnation award he purchased other property similar or related in use. The taxpayer must trace the proceeds of the award into the payments for the property so purchased. It is not necessary that the proceeds be earmarked, but the taxpayer must be able to prove that the same were actually reinvested in such other property similar or related in use to the property converted. The benefits of section 112 (f) can not be extended to a taxpayer who does not purchase other property similar or related in service or use, notwithstanding the fact that there was no other such property available for purchase.

* * * * *

STATEMENT

The facts, as found by the Board of Tax Appeals may be summarized as follows:

Petitioner Vim Securities Corporation is a corporation organized under the laws of the State of New York. It owned a parcel of real estate located at 16 Concord Street, Brooklyn, New York, which was condemned by the City of New York. The order of condemnation was entered by the Supreme Court of the State of New York on June 28, 1935, and the city took title to the property as of that date. By decree dated July 14, 1936, petitioner was awarded $90,312.50 for the condemned prop-

erty, subject to a $12,000 mortgage. When paid on October 9, 1936, the award amounted with interest to $91,604.09, of which $12,000 was used to satisfy the mortgage and $79,604.09 was received by petitioner. (R. 29–30.)

Prior to and at the time of the condemnation, the property was occupied by the Vim Electric Company as petitioner's tenant. From June 28, 1935, until the latter part of December of that year, the Vim Electric Company continued to occupy the premises under a temporary arrangement with the City of New York In the latter part of December 1935, the Vim Electric Company moved to 325–327 Gold Street, Brooklyn, New York, and it has since occupied those premises as a tenant, paying rent to the 325–327 Gold Street Corporation, Inc. (hereafter called the Gold Street Corporation). (R. 30.)

The Gold Street Corporation was organized under the laws of New York on October 1, 1935, with an authorized capital stock of $10,000 divided into 100 shares of $100 par value each. The original incorporators were Morris Borden, Anna Vinarsky, and Hyman Kaplan, each subscribing for one share of stock. Immediately after the incorporation, the original incorporators signed waivers and assigned their subscription rights, respectively, to Samuel Kassover, Julius Kassover, and Max Kassover, who, according to the minutes of the corporation, appear to have been the only

stockholders thereof. The stock certificate book of the corporation contains all certificates still in blank and indicates that no certificates of stock were ever issued from it. The record fails to show that any certificates of stock of the corporation were ever issued to anyone. The tax returns of the corporation for the calendar years 1935 and 1936 refer to Samuel, Max, Nathan, and Julius Kassover as each owning 12½ shares of the stock of the corporation. The stock of petitioner and the Vim Electric Company was owned in equal proportions by the four Kassover brothers, and Samuel was the president of both those corporations as well as of the Gold Street Corporation. (R. 31–32.)

On August 19, 1935, Julius Kassover entered into a contract with the Dime Savings Bank of Brooklyn, New York, to purchase the Gold Street property for $110,000—$10,000 to be paid upon the signing of the contract and the balance to be paid upon delivery of the deed, which was fixed for October 1, 1935. On October 4, 1935, the contract for the purchase of the Gold Street property was assigned to the Gold Street Corporation and on the same day the Dime Savings Bank deeded the property to the Gold Street Corporation. The deed was recorded on October 7, 1935, at the Register's Office, Kings County, New York. (R. 30–31.) The payments for the Gold Street property were made in the following manner: $2,000 was paid by

petitioner's check bearing date of August 13, 1935; the balance of the $10,000 deposit was paid by check of the Vim Electric Company dated August 19, 1935 (R. 32). On October 5, 1935,[1] three checks of the Vim Electric Company were drawn on the National City Bank of New York, one payable to the order of Julius Kassover, another payable to the order of Max Kassover, and the third payable to the order of Samuel Kassover, the first two being for $25,000 each and the third being for $50,000. The check for $50,000 was drawn for that amount because one of the four Kassover brothers was out of town. These three checks were endorsed to J. Kassover, who thereupon drew his individual certified check on the National City Bank of New York for $100,000, payable to the order of the Dime Savings Bank of Brooklyn, New York. This check was accepted in full payment of the balance due on the Gold Street property. On November 27, 1935, petitioner paid by check $8,000 to the Vim Electric Company as a refund for the $8,000 which it had paid the Dime Savings Bank by its check of August 19, 1935. (R. 33.)

The Board has made specific findings with respect to the manner in which the transaction was

[1] On the previous day the vendor bank had refused a tender of a certified check for $100,000 drawn by the Vim Electric Company because it did not wish to transfer title to the property to another corporation (the Gold Street Corporation) when the amount was being paid by the Vim Electric Company. This check was redeposited to the credit of the Vim Electric Company. (R. 32–33.)

treated upon the books of the three corporations (R. 34–37). For present purposes these findings may be summarized as follows: the Gold Street Corporation was treated as owning the new property and as being indebted to the Vim Electric Company for the full purchase price; interest at the rate of 5% was charged upon this indebtedness; the initial payment of $10,000 was treated as a debt owed petitioner by the Vim Electric Company.

The Gold Street Corporation filed separate income tax returns, kept separate books of account and had its own separate bank account (R. 31). In addition to the entries recording the acquisition of the Gold Street property and the indebtedness due thereon, the books of the Gold Street Corporation showed items entered under "Profit and Loss—Real Estate Taxes, Insurance, Interest on Mtges., Taxes, Depreciation." The tax returns of the Gold Street Corporation were made up from the book in which the foregoing entries appear. (R. 35.)

The admitted purpose of the organization of the Gold Street Corporation was to acquire the Gold Street property. This was done in order to conceal from the City of New York that there was being acquired another more valuable property for less money than the amount asked for the old property. (R. 31, 34, 39.)

As has been stated, petitioner received the condemnation award on October 9, 1936. It thereafter issued its checks to the Vim Electric Company as follows (R. 34–35):

Jan. 29, 1937	$20,000	May 20, 1937	$5,000
Jan. 30, 1937	10,000	June 4, 1937	10,000
Mar. 12, 1937	20,000	June 19, 1937	10,000
Apr. 29, 1937	5,000		
May 6, 1937	5,000	Total	$85,000

During the above period there were with negligible exceptions no other financial transactions between the two companies (R. 35).

The petition for redetermination filed with the Board contained no assignment of error with reference to excess profits taxes. Petitioner asserted that its "business in 1935 and 1936 was the ownership of realty and the leasing thereof to the Vim Electric Co., Inc." (R. 26.) The Commissioner's answer admitted that petitioner's business in 1936 was the ownership of realty but denied the other allegation. No reply was filed. (R. 26–27.)

In stating his case at the hearing before the Board, petitioner's counsel remarked that the question whether the corporation was doing business so as to be subject to excess profits tax "is not in the petition." On the ground that this point was not in issue, the Board sustained the Commissioner's objection to a question as to whether "petitioner did anything else for the next year after losing its building." Petitioner's income tax and excess profits tax returns state that its

business was "Owners and Operators — Real Estate", and the same answer is given in the capital stock tax return to the question, "Nature of business in detail." The income tax and excess profits tax return further states "Real estate, realty holding, real estate agents" as its "Nature of Business." Petitioner took deductions on its income tax return of $2,050.39 for attorney's fees and $25 for professional fees. (R. 27.) After the hearing it filed a motion to amend its petition to conform to the proof and brought into issue the question whether it was doing business so as to be subject to excess profits tax. This motion was granted. (R. 2, 24.)

The amount of the condemnation award exceeded petitioner's basis for the property. The Commissioner determined that the difference was taxable income in 1936 and accordingly assessed deficiencies in income and excess profits taxes. (R. 9–11.) The Board of Tax Appeals sustained the Commissioner's determination (R. 42). The circuit court of appeals affirmed (R. 72).

ARGUMENT

1. Petitioner lost its property as a result of the condemnation, but it did not "forthwith in good faith" expend the proceeds of the award "in the acquisition of other property * * * or in the acquisition of control of a corporation owning such other property," as required by Section 112

(f) of the Revenue Act of 1936. Indeed, so far as the record shows, it never acquired any other property to replace that which had been condemned.[2] It is true that the Gold Street Corporation did acquire similar property, but the Gold Street Corporation was a distinctly separate entity and may not be ignored at petitioner's behest. On this point the court below has followed the plain and unambiguous rule stated in *Higgins* v. *Smith,* 308 U. S. 473, 477, as follows:

> * * * A taxpayer is free to adopt such organization for his affairs as he may choose and having elected to do some business as a corporation, he must accept the tax disadvantages.

The rule of that case has been widely applied. See, *e. g., Commissioner* v. *Moline Properties* (C. C. A. 5th), decided November 7, 1942 (1942 Prentice-Hall, par. 63,018), reversing 45 B. T. A.

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[2] It is clear that petitioner never acquired control of the Gold Street Corporation. It did not acquire a single share of the stock of either the Vim Electric Company or the Gold Street Corporation. It failed even to satisfy the trier of fact that the stockholders of the Gold Street Corporation were the same as its own and those of the Vim Electric Company. (R. 40.) Article 45–1 of Treasury Regulations 94 (Pet. 10–11) lends no support to petitioner. That regulation is interpretive of a section of the statute which gives the Commissioner authority to make his own allocation of income among organizations controlled by the same interests in order to prevent the evasion of taxes. Those provisions obviously have no relation to any question here involved.

647; *Interstate Transit Lines* v. *Commissioner,* 130 F. (2d) 136 (C. C. A. 8th); *Texas-Empire Pipe Line Co.* v. *Commissioner,* 127 F. (2d) 220 (C. C. A. 10th); *Watson* v. *Commissioner,* 124 F. (2d) 437 (C. C. A. 2d).

If there are situations in which the rule of *Higgins* v. *Smith* does not apply, the instant case is certainly not one of them. The Gold Street Corporation was organized for the specific purpose of acquiring title to the new property, so that there could be concealed from the city the fact that a more valuable parcel of property was being acquired for less than the amount which was being claimed in the condemnation proceedings (see Statement, *supra,* p. 8). Not only was that purpose achieved, but it was apparently deemed desirable to continue the Gold Street Corporation after the condemnation proceedings had been completely terminated. There can be no unfairness therefore in treating the corporation as an existing, distinct entity. Moreover, the separate state of the corporate entities was scrupulously observed by the parties throughout all the transactions among the three corporations, and even more significantly, this was recognized in the income tax returns filed for the three corporations. Rent paid by the Vim Electric Company to the Gold Street Corporation was not reflected in the income of petitioner Vim Securities Corporation. The interest

charged to the Gold Street Corporation in 1937 was credited to the Vim Electric Company and not to petitioner. (See R. 35–36.) The Vim Securities Corporation has therefore insisted upon the separate identity of each corporation for all purposes including those of the federal income tax, with the exception of its contention in this case. These factors sharply distinguish the instant case from *United States* v. *Brager Building & Land Corp.*, 124 F. (2d) 349 (C. C. A. 4th), and *North Jersey Title Ins. Co.* v. *Commissioner*, 84 F. (2d) 898 (C. C. A. 3d).[3] It is true that in both those cases the corporate entity was disregarded at the behest of the taxpayer, but in each of them the taxpayer sought to have the corporation disregarded for *all* purposes of the federal income tax. Moreover, the *North Jersey Title Ins. Co.* case was decided prior to *Higgins* v. *Smith*, and the *Brager* case would probably not be followed in the Fourth Circuit since the reversal of its decision in *Powell* v. *Gray*, 114 F. (2d) 752 (C. C. A. 4th), in which this Court stated (314 U. S. 402, 414): "The choice of disregarding a deliberately chosen arrangement for conducting business affairs does not lie with the

[3] The court's disregard of the corporate entity in *Munson S. S. Line* v. *Commissioner*, 77 (F.) 2d 849 (C. C. A. 2d), was based upon the construction of the language and purpose of a special statute enacted to encourage the development of an American merchant marine.

creator of the plan. *Higgins* v. *Smith,* 308 U. S. 473, 477."

Even if it should be thought that there is still some question concerning the applicability of the rule of *Higgins* v. *Smith,* this case does not present a proper vehicle for determination of the question. For, as both the court below and the Board of Tax Appeals have held, the result reached is sustainable upon wholly independent and unimpeachable grounds. The regulations specifically authorized by Section 112 (f) provide that a taxpayer who seeks to come within that section must trace the proceeds of the award into the payments for the new property and must be able to prove that the proceeds were actually invested in it. In the instant case, payment for the new property was completed on October 5, 1935, and the award was not received until more than a year later, October 9, 1936 (see Statement, *supra,* pp. 5, 7). Manifestly, the proceeds of the award could not have been used to acquire the new property and Section 112 (f) is therefore inapplicable. *Bandes* v. *Commissioner,* 69 F. (2d) 812 (C. C. A. 2d). Moreover, those proceeds were not even distributed to the Vim Electric Company (which had advanced the purchase price of the new property) at the time of their receipt by petitioner. The first payment by petitioner to the Vim Electric Company was not made until almost four months after the receipt of the award, and the payments were

extended over a period of approximately five months. No explanation was offered for this delay (R. 39) and, as the court below pointed out (R. 71), "In the meantime, so far as appears, it retained the proceeds of the award and may for all that we can know have used them for general business purposes."

2. No question concerning the construction of the excess profits tax imposed by Section 106 (a) of the Revenue Act of 1935 is presented by this case. The opinions below do not decide that a corporation which neither owns nor operates property is carrying on or doing business within the meaning of that tax. The Board held that petitioner failed to prove that it neither owned nor operated property (R. 27–28). Furthermore, the record discloses that no issue was made in the pleadings before the Board upon this question; and the Commissioner's determination that petitioner was doing business was presumptively correct. *Welch* v. *Helvering,* 290 U. S. 111, 115. The decision of the circuit court of appeals is merely that the Board did not commit error in sustaining an objection to a question upon this point asked at the hearing, since it was not in issue in the case (R. 71).

CONCLUSION

The decision below is correct. There is no conflict upon either of the issues involved, and there

is therefore no occasion for further review. The petition should be denied.

Respectfully submitted.

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